



MINUTES

LOSS TRUST FUND BOARD MEETING 7447 E. Indian School Rd., Suite 210 Finance Conference Room Scottsdale, AZ

**December 12, 2012
3:00 p.m.**

PRESENT: George Hostal, Chair
James Tomlinson, Vice Chair
David Petulla
Bill Powell
Jim Stabilito

STAFF: Ted Howard, Risk Management Director
Jack Shafer, Assistant City Attorney
David Smith, City Treasurer
Joyce Gilbride, Financial Services
Gina Kirklin, Enterprise Finance Manager
Gloria Moore, Financial Services
Judy McIlroy, Financial Services
Ken Nemec, Human Resources Benefits Manager

OTHER Charlie Broucek, Hays Management Consulting

1. CALL TO ORDER

Chair Hostal called the meeting of the Loss Trust Fund Board to order at 3:07 p.m.

2. ROLL CALL

A formal roll call confirmed the presence of all Board Members as stated above.

3. OLD BUSINESS

1. Approval of the March 15, 2012 Minutes

VICE CHAIR TOMLINSON MADE A MOTION TO APPROVE THE LOSS TRUST FUND BOARD MINUTES FOR THE MARCH 15, 2012 MEETING. BOARD MEMBER PETULLA SECONDED THE MOTION, WHICH CARRIED BY A UNANIMOUS VOTE OF FIVE (5) TO ZERO (0).

4. NEW BUSINESS

1. Introduction of new Board Member

Mr. Ted Howard, Risk Management Director, introduced the new Board Member, Mr. Jim Stabilito. Board Member Stabilito described his background in insurance and risk management, with a focus on health and welfare and workers compensation.

2. Ethics Refresher Training

The ethics refreshing training video was screened and Board Members completed the personal interest disclosure forms and the public services training forms.

3. Administrative review of the Risk Management annual report

Mr. Howard provided a PowerPoint presentation of the FY 2011/2012 annual report. Although the City's operating budget decreased by 7 percent, the total cost of claim payments, operating expenses and excess insurance premiums increased by 35 percent. He pointed out that part of that increase is due to an accounting anomaly which will not be repeated. The premiums for both FY 2011/2012, the prior fiscal year, and for FY 2012/2013 were paid during the year.

Vice-Chair Tomlinson inquired why the FY 2012/2013 premium had been paid earlier than it customarily has been. Ms. Joyce Gilbride, Director of Accounting, said her understanding was that the invoice had been submitted to accounts payable, perhaps during the transition of risk management directors. By the time this anomaly was discovered the insurance company had already cashed the check. They have taken steps to ensure that this does not happen again.

In further discussion, Board Members concurred that although an exact percentage for the true cost of risk had the second premium not been paid in FY 2011/2012 is not currently available, the percentage would probably be around 1.4 percent. Board Member Powell asked how the target goal for the City's cost of risk of two percent was set.

Mr. Howard said this was set previously by the City. Citing his experience with the County, their goal had been one percent. City Treasurer David Smith said this is an internal City policy or guideline rather than a policy of the Loss Trust Fund Board. Chair Hostal requested that a discussion of this topic be agendized for the Board's next meeting.

BOARD MEMBER POWELL MADE A MOTION TO AGENDIZE A DISCUSSION OF WHAT THE TARGET GOAL FOR THE CITY'S COST OF RISK SHOULD BE. VICE

CHAIR TOMLINSON SECONDED THE MOTION, WHICH CARRIED BY A UNANIMOUS VOTE OF FIVE (5) TO ZERO (0).

Board Member Powell noted that medical payments associated with denied workers compensation claims are included in the cost of risk. He asked how that happens. Mr. Howard explained that disputed worker's compensation claims have been settled by a payment, with the agreement that the claim is non-compensable and benefits are denied.

Board Member Stabilito asked what the target reserve is for FY 2011/2012. Mr. Smith explained that there are substantial reserves in the program.

Chair Hostal asked Mr. Howard if he feels the reserves are adequate. Mr. Howard replied that a further review of all pending claims is necessary and that the reserves might be increased as a result of that. He added that his assessment is that they need to pay further attention to pending claims. They are currently recruiting for an experienced claims adjuster to work on liability and property and have found a highly qualified candidate. Once the person is on board he anticipates that this will be of great assistance to him in evaluating all the pending claims. Chair Hostal said this position will likely pay for itself. Mr. Howard agreed and said that this will lead to more timely evaluations and settlements which will drive down claim costs. This will give the City a better picture of what reserves are needed and better control litigation expense. Recoveries should also be improved.

Mr. Howard explained that he will be conducting a full review of the workers compensation pending claims, but his preliminary impression is that this area is being managed properly. Board Member Powell commented that the medical bill review savings is outstanding and the City should be commended on the savings achieved by using a third party bill review vendor. Mr. Howard said the workers compensation adjuster deserves the credit for this.

Mr. Howard said he anticipates increased recoveries in the property liability area over the next few years as the new claims adjuster comes on board.

Reviewing the six year overall loss performance data, Mr. Howard admitted he does not know the full history of what caused the City to incur some of the expenses in FY 2008/2009.

Chair Hostal said the six-year average is approximately \$2.6 million, although the average for the last three years has been around \$1.3 million. This is a significant difference. As they look at projections he urged them to keep this fact in mind. The history for the last three years seems abnormally good.

Board Member Powell said the OSHA frequency and severity rates in the fire and police departments is a big contributor to the overall cost of risk. He asked how that compares to similar municipalities. They benchmark overall claims to other municipalities, but if the problem is the fire and police departments, he would like to see a direct comparison with other municipalities. Depending on those results, he might also want to know what the City is doing to prevent and control losses. Mr. Howard said he has experience with law enforcement claims with Maricopa County. Their expenses were far higher. The jail operation in itself is a substantial exposure. He opined that based on his experience, the

Scottsdale Police Department is doing very well. However he undertook to do some benchmarking, at Board Member Powell's request. Chair Hostal noted that this exercise might need to include municipalities outside of the Valley with similar demographics.

Mr. Smith noted that the fire and police departments had shared a fitness and wellness coordinator, who had done an outstanding job. That individual has left the City, however. Mr. Howard said that the position has been posted. It is funded through the Risk Management Department. Chief Rodbell is very concerned about safety.

Mr. Howard said that for forecasting purposes they consider the six-year history. Other factors they consider include pending claims and when they are likely to settle.

Mr. Howard reviewed the financial forecast for the Risk Management Self-Insurance Fund.

Board Member Petulla asked about the recoveries. Mr. Howard explained that there are two components and they use different accounting methods. For next year, his department will work with Financial Services to articulate them. Board Member Petulla said he was trying to relate this information to the information on claims data presented on page 12 of the report. Mr. Howard said there are also timing differences. Board Member Powell asked if this is because the data on page 12 does not include the risk management operating budget. Discussion ensued. Chair Hostal pointed out that the information on pages 7 through 12 is not consistent with the information on page 2. Mr. Howard said he had been looking at different figures and agreed that the timing issue does not explain everything. Going forward the report will be changed to reflect and make the comparisons easier.

Board Member Powell said this relates to loss performance. Excess insurance premiums are not considered loss performance, so that amount is probably not embedded in the figure at the bottom of page 12. Mr. Howard agreed that it is not. Board Member Powell said the \$2.4 million of excess premiums would account for the difference. Mr. Howard explained that the excess insurance premiums are broken out of the claims on the financial forecast. They are also broken out of the cost of risk analysis.

Board Member Powell asked whether the excess insurance premiums are factored into the numbers that appear on page 12. Mr. Howard confirmed that they are not. Board Member Powell said this explains the discrepancy. Board Member Petulla said on page 12 each year stands alone. Mr. Howard said the six-year overall loss performance is shown the same way as in the past. The frequency of claims should match up.

Chair Hostal suggested that in the future, claims paid in the current year that relate to the current year be shown for each of the four subcategories. Then another section should be inserted showing general liability claims from prior years paid in the relevant fiscal year. As they plan for the future, if there are known claims that may lead to future payments, the report should include projections of existing claims. This would enable the Board to oversee this information. He added that the Board has been concerned by the dramatic drop in reserve levels, from \$19 million to \$13 million. As citizens the Board Members want to hold firm so that the reserves are not used to maneuver the budget.

Board Member Petulla asked Mr. Howard whether claims paid in the current year on past claims would mean that the numbers paid in the past would be adjusted. Mr. Howard said they would be and undertook to verify whether this in fact happened.

Board Member Powell said even if a claim is recorded in FY 2009/2010, if it is not entirely paid out in that fiscal year, when is that information shown? Different organizations handle this differently. Mr. Howard said for the purposes of comparison and trending they would want to identify the payments made on claims in the year they were reported. Board Member Petulla said he wanted these figures updated every year. Mr. Smith said one advantage of seeing the reserve number against what is actually paid over time is that they can get confidence in the adequacy of the reserves. Mr. Howard said the purpose of these slides in the presentation was to compare year to year loss experience. Mr. Smith added that \$1 million was moved into the health care fund, and the reserves were purposely reduced by a further \$1 million in FY 2011/2012. One cannot address the question of the reserve levels without reference to the actuarial levels.

Board Member Stabilito asked whether there was pressure from the City to reduce the reserves. Mr. Smith said the reserve fund cannot be used as a piggybank for the City. There was never any intention to deplete the reserves and move the funds to the General Fund.

Mr. Howard said the ending balance in the reserve was \$15 million, which is in excess of the 90 percent confidence level. Mr. Smith reminded the Board Members that historically they have shot for the 80 percent confidence level. Chair Hostal commented that in fact they had been well above the 90 percent confidence level for the years preceding these changes. Chairman Hostal said his biggest concern is that for FY 2012/2013 the City's adopted revenue is \$4.8 million, now forecast at \$4.6 million, which is \$1 million less than the \$5.5 million actual for FY 2011/2012. The amount for FY 2013/2014 is \$7.15 million. He is concerned about the City's appetite for additional costs of \$2.5 million. Over the next five years that totals \$12.5 million. The total ending fund balance forecast for FY 2017/2018 is \$13.8 million. If the \$12.5 million is subtracted from that ending balance, the FY 2017/2018 reserve would be \$1.3 million, which is below their confidence level. He is concerned that the City will not automatically adopt the \$6.5 million without question, as \$2.5 million is approximately one percent of the City's annual budget. He would prefer to stay at the 90 percent confidence level. Five years from now the current forecast shows a reserve at the 75 percent confidence level, but assumes a revenue increase that to him seems unrealistic.

Mr. Smith explained that the \$6.5 million internal rate forecast for FY 2013/2014 is the same figure as was used for FY 2010/2011. The intervening years are anomalous, where the Board aimed to reduce the reserve from \$19 million. He argued that if they return to the historical levels, they project an ending fund balance of \$13 million, which is in the 85 to 90 percent confidence level. Adjustments will be made annually going forward. He would have little tolerance for any pushback from the City regarding the premium of \$6.5 million. This means they are getting the program back to where it was.

Mr. Howard said that in regard to the claims on the general liability side, they built in some increases over the forecasted years. He believes they will spend that money. He predicted the City's claims history will trend up on the general liability side. They have taken the advice of their insurance broker regarding general liability premiums. On the workers compensation side there are some concerns about the condition of the work force, specifically the fire department, which have been addressed with increases on the workers compensation side. If the loss experience is better than anticipated that will give some relief on the fund balance side and they will not need to collect at those rates.

Chair Hostal asked Mr. Howard about the forecasts. Mr. Howard said he did not want to discuss specific pending cases.

Mr. Smith added that while expected claims are forecast at around \$2 million annually, on the revenue side he reminded the Board that by law, large tort claims can be added to the property taxes. In the forecast, staff has taken the position that City Council may not agree to do this. Therefore the forecast is very conservative.

Benefits Manager Mr. Ken Nemec presented the health care portion of the annual report. He reviewed the history of the City's self-insured medical and dental plans and noted that only about 18 months remains on the City's current contract with Aetna for the medical plan. Staff plans to put the life, disability and some other insurance plans out for bidding early in 2013 in order to proactively manage them and focus on the health insurance plan later.

Last July the City added a health savings account to the high deductible PPO plan. The City has not been contributing to the HSAs, although he acknowledged that many employers do.

Mr. Nemec discussed the actuarial results. Claims paid out exceeded revenue by \$2.4 million in FY 2011/2012. He noted that in both FY 2010/2011 and FY 2011/2012 the plans were underfunded. This was partly because administrative expenses and health and wellness program expenses were not included in the amount being charged to employees. The second source of underfunding was that after several years of very favorable claims experience, late in FY 2010/2011 health care expenses jumped and this continued through FY 2011/2012, with more chronic conditions and more catastrophic claims. A third factor was that about three years ago the health care reserve was as high as \$8 million. The City gave a \$4 million premium holiday shared between the City and employees.

Mr. Nemec reviewed current and future plans. Last year premiums were increased by 17 percent to employees and 80 percent to retirees. Ten catastrophic claims were incurred which each reached at least one-half of the stop loss deductible. This resulted in payments of \$2.3 million, representing roughly ten percent of the losses.

Board Member Powell asked if staff will revisit the aggregate stop loss. Mr. Nemec replied that they stopped looking for aggregate stop loss about five years ago. Board Member Stabilito said it is uncommon for employers to buy aggregate stop loss in these circumstances. His personal opinion is it would be a waste of money. Mr. Charlie Broucek of Hays Management Consulting concurred.

Mr. Smith said the City does not have an actuary who evaluates the City's health insurance risks. They take into consideration the volatility of claims experience and add a factor to that.

Chair Hostal commended staff for doing a great job in this regard over the last couple of years. Today only 98 retirees have stayed with the City plan, down from 278 before the rates were raised, putting Scottsdale on a par with neighboring municipalities. Mr. Smith interjected more retirees are expected to switch to the State program on January 1. Chair Hostal asked whether the larger claims are expected to decline, given the drop in the average age of people enrolled in the City plans. Mr. Broucek agreed there is a

significant difference in the risk factors. Chair Hostal asked staff if they feel comfortable with the reserve figures. Board Member Stabilito added that the time it takes to process a claim will need to be analyzed. He said that a reserve of 15 percent of expected claims is solid from an industry standpoint. Mr. Broucek said he is comfortable with the reserve.

Mr. Nemec discussed the forecast for FY 2012/2013. Revenue forecasts could be high because more retirees than predicted are leaving the City plan. However this will also mean lower claims. Four months into the year they are close to what they predicted. In response to a comment by Board Member Petulla about the lower expenses for the wellness program, Ms. Gloria Moore of Financial Services noted that the cash incentive is no longer offered to employees. Mr. Nemec said at the inception of the program there were some capital improvements to build fitness facilities. This is no longer an ongoing expense. Also the workforce has shrunk, which means fewer employees participate in the programs.

Board Member Petulla pointed out that again it seems as if the retirees' claims are higher than the premiums they are paying. Mr. Smith said even if more retirees migrate to the State pension plan it will probably never drop to zero, and it will probably never balance the claims because Council agreed to continue subsidizing premiums for disability retirees. Board Member Stabilito cautioned that as the size of the retiree pool shrinks the likelihood of being able to balance the premiums and claims becomes even more remote. He pointed out that even after some have left in January, over 2013 the City will still have claims to pay that have already been incurred.

Mr. Nemec summarized that for future year forecasts their goal is to break even with projected cost increases of 8 percent. Board Member Powell inquired about a confidence level for the Health Care Fund. Mr. Nemec said it does not have an actuarial confidence level. Mr. Smith said the reserve level is appropriate for the size of the program.

Chair Hostal asked about the percentage of premiums paid by the City and the percentage paid by employees. He recalled that research last year showed that Scottsdale was one of the more generous municipalities in the Valley. Mr. Nemec said some of the cost has been shifted back to employees. The City is closer to the Valley norm now. Mr. Smith said they will likely be recommending an across the board premium increase of 8 percent for both the City and the employees. Mr. Broucek said 8 percent is probably a worst case scenario. He added that the projections do not include the cost of healthcare reforms and taxes. He is working to determine exactly what the City's responsibility will be for the reinsurance tax. Mr. Smith confirmed that this would total approximately \$360,000.

Chair Hostal said staff are to be applauded for being on top of this issue. He asked that when staff presents recommendations to Council that they try to factor everything in, keeping in mind where they are and the fact that they are still slightly below the Valley average relative to cost per employee. Scottsdale wants to remain an employer of choice.

MOTION TO ACCEPT THE ANNUAL RISK MANAGEMENT REPORT AS PRESENTED WITH THE EXCEPTION OF THE ITEMS MENTIONED DURING THE MEETING TO MODIFY THE REPORT IN FUTURE YEARS, BY BOARD MEMBER

POWELL. VICE CHAIR TOMLINSON SECONDED THE MOTION, WHICH CARRIED BY A UNANIMOUS VOTE OF FIVE (5) TO ZERO (0).

4. Discussion and possible approval of establishing the schedule of future Loss Trust Fund Board meeting dates for the remainder of calendar year 2013

The Board Members agreed they prefer to meet at 8:00 a.m.

Mr. Howard noted the need for a meeting in late January or early February to discuss recommendations about the health care plan to be forwarded to City Council. The Board decided to meet on Thursday, January 31, 2013 at 8:00 a.m.

Mr. Howard asked how frequently the Board wished to meet. Mr. Smith suggested holding quarterly meetings now that the Board oversees a bona fide trust it has a different level of responsibility. In ensuing discussion, the members agreed that this makes sense but that the exact timing of meetings throughout the year would match staff's need for their input.

MOTION BY CHAIR HOSTAL TO HOLD QUARTERLY MEETINGS OF THE LOSS TRUST FUND BOARD, BEGINNING WITH THE MEETING TO BE HELD JANUARY 31, 2013, AT 8:00 A.M. BOARD MEMBER PETULLA SECONDED THE MOTION, WHICH CARRIED BY A UNANIMOUS VOTE OF FIVE (5) TO ZERO (0).

OPEN CALL TO THE PUBLIC

No members of the public wished to address the Board.

ADJOURNMENT

With no further business to discuss, being duly moved and seconded, the meeting adjourned at 5:03 p.m.

Respectfully submitted,
A/V Tronics, Inc. DBA AVTranz